

Can You Survive the Ebay Economy?

If you think Web auctions are only for collectibles, you're in for a surprise. These online agoras now sell everything from moving services to real estate while giving rise to "microbusinesses," a new and increasingly powerful type of enterprise.

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Online auctions aren't just for collectibles anymore. They're selling everything from moving services to real estate -- and they may be muscling into your turf.

Online watch retailer Grandwatches sells Omega, Seiko, and other quality brand-name watches at steep discounts not only on its own Web site but also on eBay's and Yahoo's online auctions. The discounts are possible because Grandwatches operates with gross margins ranging from 1% to 12%, compared with as much as 50% at traditional jewelry stores. How does the company get by with such razor-thin margins? Low overhead, of course. In fact, overhead can't get much lower than it does at Grandwatches. The company consists of only Omar Nuno, a full-time Medicare claims processor at HMO Kaiser Permanente in Pasadena, Calif., who stays up late at his home computer putting up listings for new merchandise and trading e-mail with his customers. "It takes me a couple of minutes to put up another watch," notes Nuno. "I have a vacation coming up, so I should have time to double my listings."

Nuno's company is an example of a class of tiny enterprises -- call them "microbusinesses" -- that have come into their own online and may well be giving conventional small businesses a run for their money. The Web was supposed to level the playing field between large and small companies. It hasn't, because small companies' Web sites have been buried out of view from consumers in a sea of competitive entries. Large companies, meanwhile, whether they're conventional corporations fortified by brick-and-mortar sales or dot-coms wielding vast piles of cash hurled at them by giddy investors, are buying eyeballs via massive advertising campaigns. But what the Web has done is level the playing field between small businesses and the micro-businesses that until now barely showed up on anybody's radar screen.

Those microbusinesses are individuals without a substantial -- or in many cases, any -- business history or infrastructure behind them. Operating with virtually no overhead, typically with little inventory, and sometimes in legal gray zones, these one-person shows are often able to offer fire sale prices and still maintain a modest margin. And the billions of dollars in revenues that they in aggregate are piling up come, to a certain extent, out of the coffers of more traditional businesses.

The market

Microbusinesses are tapping into powerful markets. Grandwatches' Nuno, for instance, has sold watches to customers in Belgium and Japan. Another example is Ed Ciliberti, a Pacific Grove, Calif., real estate broker who three years ago opened a booth at a local antiques mall. It was a pleasant hobby, but he wasn't clearing much. Last September he tried his hand at selling on eBay, and within three months he had earned about \$30,000 on sales of \$70,000. An antique peanut roaster that he'd bought for \$250, and that failed to sell at the mall or at local auction, went for \$2,950 on eBay. A copy of the first issue of *Playboy* magazine, which he'd bought for \$900 and had autographed by Hugh Hefner, went for \$11,100. Now he spends 60 hours a week online, whereas his real estate activities have been pruned back to 15 hours.

Although the major online auctions have long been known for collectibles, an important change has quietly taken place during the past year or two: the auctions have become popular conduits for everything from real estate to automobiles. "This isn't the tchotchkes business," says **Tony Surtees**, general manager of the Commerce Group at Yahoo, which runs the second-largest online auction. EBay, the granddaddy of online-auction sites, lists more than 130,000 computer items and 6,000 cameras. "We have never wanted to limit ourselves in any way, shape, or form to the collectibles market," says Brian Swette, eBay's chief operating officer. As a sign of the times, he notes, the company plans to relabel its thriving "sports memorabilia" section as simply "sports" to reflect the fact that collectibles are being shouldered aside by "practicals."

Still, Swette and other eBay employees refer to their site as a trading community, apparently to preserve the notion that the online auction has more in common with swap meets than with malls or other retail outlets. "We offer something more personal, more special," says Swette. "Almost every item has some level of uniqueness to it."

Really? I did a few quick searches of eBay and came up with the following counts of listings: 295 for screwdrivers, 65 for guitar strings, 108 for staplers, more than 7,000 for sweaters, 4 for disposable diapers, and 10 for hamster cages. Throw in countless watches, cameras, and baseball cards, and that short list places eBay in direct competition with almost every retail store in the downtown area of the midsize suburb in which I live.

There is certainly no shortage of buyers. On any given day about 1.5 million people visit eBay, which lists close to 4 million objects. According to Forrester Research Inc., in Cambridge, Mass., online auctions got \$1 billion out of consumers in 1999, and the firm predicts that that number will rise to \$19 billion by 2003.

As for sellers, none of the online auctions release a detailed breakdown, but eBay's Swette says that there are hundreds of thousands of casual sellers on eBay who pull in less than \$2,000 in auction revenues a month, and at least 25,000 "power sellers" who rake in from \$2,000 to \$500,000 a month.

Who are those power sellers? Again, the auctions themselves don't give out details. But Munjal Shah, CEO of Andale Inc., a company in Santa Clara, Calif., that provides financial and other services to high-volume online-auction sellers, claims that about 60% of all power sellers are conventional businesses that have opened up online-auction arms, often after having struck out with their own Web sites. That was the case with Marcello Veloso, who opened his Natick, Mass., sports card store eight years ago. But the business really took off, he says, when he started selling cards on eBay, two years ago. He's kept the store, largely because it provides a handy facility for auction surfing, inventory storage, and shipping. "Right now," Veloso says, "the money is on the Internet."

The other 40% of power sellers, says Shah, are individuals. Why are so many people creating one-person businesses focused on online auctions? Because they can. "The online-auction markets are creating the lowest barrier to entry that has ever existed," says Shah.

Microbusinesses could even spring up in the rapidly growing business-to-business auction market. I went to Bizbuyer.com's Web site, spent about three minutes filling out a form to register as a moving company -- sure, I had liability insurance, and no, my state didn't require a license -- submitted it, and a moment later found a "You have buyers!" button waiting for me. Clicking on it brought up an invitation to bid on moving a 50-employee telecommunications company from Massachusetts to Alabama. If I had gone on to bid and won the business, I suppose I could have subcontracted the job out or rented a truck and hired some college students with moving experience. Voilà: instant commercial mover.

The competitive advantages

For anyone who wants to remain with a business old-fashioned enough that it encompasses such relics of the pre-eBay era as employees, offices, showrooms, catalogs, and the like, it's worth considering what one is up against in microbusinesses.

eBay's Swette estimates that an individual power seller achieves from 5 to 15 times the return on assets that a conventional small business does. No wonder: Not only do power sellers avoid major sources of overhead, but since many of them work from their homes, they often can take more tax deductions as well. And there is widespread recognition that many aren't paying all sales and income taxes on their online take. "At the antiques mall, everyone had to have a resale license, and the mall took out sales tax," says Ciliberti, the online antiques seller. "Online I don't have to pay taxes on sales outside of California, and there's nothing the state can do about it."

If, despite a low or nonexistent overhead, decent profits still manage to elude a microbusiness, that's not necessarily a showstopper. Since many microbusiness founders are part-time entrepreneurs or have gainfully employed spouses, they can in effect operate like miniature dot-coms, allowing other sources of cash to subsidize the low prices they need to offer to undercut conventional businesses.

If they do make a profit, eBay won't take much of it: a listing fee ranging from 50¢ to \$2 and a final-value fee based on the winning bid's sales price -- 5% of the first \$25, plus 2.5% of the amount from \$25 to \$1,000, plus 1.25% of the amount over \$1,000. (The fees for automobiles and real estate are higher.) Amazon.com and Yahoo, meanwhile, charge sellers nothing for auction listings (in hopes of drawing businesses away from eBay). At his local antiques mall, in contrast, Ciliberti was paying \$550 a month for his booth plus a 10% commission on all sales.

Besides not needing money to plunge into online auctions or cyberboutiques, microbusinesses also don't need any operational expertise. Companies like Andale set up auction listings, process credit card payments, and help with accounting and inventory management, all for a modest fee. Amazon's cyberboutiques, which the company calls "zShops," come with a button that allows many of Amazon's more than 15 million customers to charge an item in the boutique to their credit cards with a single click. The cost for a zShop: \$10 per month and 5% or less of the sale price. "You don't have to touch product or invest capital to get into this business," says Andale's Shah.

Think that customers' concerns about getting ripped off by a fly-by-night auction seller will keep them coming to your store? Don't count on it. The feedback system pioneered by eBay -- and imitated by Amazon, Yahoo, and others for their auctions -- provides a simple and convincing means for determining at a glance whether a seller is trustworthy. It works like this: if a seller does anything to annoy a buyer, the buyer can give the seller a black mark that lowers the seller's prominently displayed rating. Buyers who are still hesitant can use inexpensive escrow services like i-Escrow Inc., which will hold onto a buyer's payment until the purchased item has passed the buyer's scrutiny. eBay offers buyers up to \$175 worth of insurance at no charge, and Amazon guarantees its zShop customers satisfaction on purchases up to \$1,000.

A brick-and-mortar store has to build an identity in the public's mind and then make sure it has products on hand to back up that identity. Microbusinesses, in contrast, with their ultrafast inventory turnover and automatic exposure to potential customers through product listings, can leap opportunistically from market to market without penalty. Veloso, the sports card seller, jumped into the Beanie Babies market before it peaked, made a killing, and then jumped out when it flattened and on into the then-nascent Pokémon market. "The online world gives the little guys the flexibility to change their entire inventory overnight," says Robert Robicheaux, a professor of retail marketing at the University of Alabama.

As for marketing, microbusinesses gain intimate, precisely targeted access to the largest aggregation of shoppers in the history of humankind, and at virtually no cost. On the online auctions or in the cyberboutiques, sellers are essentially guaranteed that their product listings will pop up in front of interested buyers on a more or less equal basis with those of larger businesses with large overheads. It doesn't take much photography or copywriting expertise to create maximum appeal within a listing.

There's one other marketing edge a microbusiness can exploit, and from the point of view of conventional small businesses it might be considered an especially insidious one. That's the ability to penetrate the Internet's somewhat guarded network of virtual communities -- the message boards, chat rooms, and e-mail lists that millions of people use to make friends, swap information, and let off steam.

Nick Mannarino, president of Modern Performance Inc., in West Long Branch, N.J., has found himself up against that edge. Mannarino has been a longtime contributor to an e-mail list of 800 enthusiasts of Merkur, a German-made sports sedan imported to the United States in small numbers by Ford in the mid to late 1980s. Modern Performance provides custom components for Merkur. Last year a rather heated debate on the merits of one of the components all but took over the list for several days, but Mannarino, who not surprisingly knows more about the workings of the component than any other human on the planet, was utterly silent. He had to be; according to the list's rules, he says, businesses aren't allowed to plug their products in any way. That's a standard rule of most electronic communities -- and he knew from personal experience that the Merkur list's moderator applies the rule strictly. So he kept his mouth shut.

That enforced silence was particularly frustrating, notes Mannarino, because several of the people who had weighed in against the component -- or against other components sold by Modern Performance and other specialty manufacturers -- sell competing products. Some of those enterprising list members scavenge and recondition parts from junkyards, others make their own, and some buy them from manufacturers. Not only can the resulting products be found on Web sites, on online auctions, and in cyberboutiques, but in many cases they are openly advertised in messages on the mail list. Those people are running microbusinesses, of course, but because they don't wrap themselves in the formal trappings of a real business, they slip in under the community's radar and get to market directly to the most highly select audience imaginable, at zero cost.

Microbusinesses are using such marketing ploys in virtual communities Internet wide. Says Robicheaux: "A business has to spend a few thousand dollars getting a mailing out, while others can spend a few hours in a chat room reaching thousands of people for free."

The entire world of online auctions and related microbusinesses is still rather small, accounting for perhaps 1% of annual U.S. retail sales. Relatively few owners of conventional businesses perceive their existence to be imperiled by online microbusinesses. But that will change if online auctions and cyberboutiques continue to grow explosively. The popularity of microbusinesses may have already begun to tilt the playing field away from even Web-savvy small businesses by rendering irrelevant many of their competitive advantages, turning their cost structures against them, and excluding them from the powerful new forms of online marketing wide open to microbusinesses. We may increasingly find ourselves living in a sort of "eBay economy," in which small businesses face tremendous pressure either to invest heavily in sharply distinguishing themselves or to dramatically shed costs and switch competencies to beat microbusinesses at their own game.

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Online Auctions: A Shopper's Delight

Like many shoppers, I'm willing to pay at least a small premium for the opportunity to buy locally. But occasionally, certain advantages of shopping online prove irresistible. For example, my wife and I recently bought a sleeper sofa from an online retailer because the delivered price was several hundred dollars lower than the price of any similar sofa we found in brick-and-mortar stores. We also do most of our grocery shopping online, saving us an hour or so of hassle every week.

Another advantage of online shopping can be selection. That was the lure recently when I became interested in a particular diving watch, a Citizen product called the Aqualand. Though it's not a rare or an exotic watch, it's apparently specialized enough to fail to warrant shelf space at any retailer within striking distance of my home. So I hit the Internet.

Surprisingly, an "Aqualand" search on AltaVista turned up only one slick comprehensive watch site of the sort that might reasonably be called a dot-com operation. The price at that site for the particular model of Aqualand I was interested in was \$446.25. However, the search also turned up a few listings for boutique-type online shops, all of which had Yahoo addresses. Taking the hint, I went to Yahoo and searched its own internal shopping listings. Up popped 89 listings among Yahoo's "cyber-boutiques" -- low-cost sites on which anyone can list products at fixed prices -- where prices for the watch dipped as low as \$300. But Yahoo also alerted me that Aqualands were being offered at its online auctions. I checked out their listings and similar listings at the other major online auctions.

I immediately discovered that among all the purchasing channels available to me, the real deals in Aqualand watches lay with those auctions. EBay had 19 of them for sale; Yahoo, 3; Amazon.com, 5. A few of the listed watches were

used, but most were described as brand-new, in-the-box, warranted merchandise, and some were going for less than \$250. Some of the sellers seemed to be brick-and-mortar shops, whereas others seemed to be storeless individuals, but in most cases it was hard to tell exactly who or what the sellers were. All the listings had the same basic format, so that one from the Sharper Image wouldn't necessarily have been any more prominent or slicker than one from an enterprising retired grandmother in South Bend, Ind.

Retail Holdouts -- But at What Price?

"I hate the online world," says Don True, the amiable owner of Country City Store, a cluttered shop tucked away on a quiet, mostly residential street in Manhattan's trendy East Village. "It's impersonal. Some of my customers talk about buying antiques online, but most of them come back to me. I think the prices aren't that good on eBay, and people are afraid of ending up with a piece that's chipped."

Down the block is Bernd Goeckler Antiques, a more spacious store where the antique-furniture prices run into the tens of thousands of dollars. No aversion to technology here: two large thin-screen monitors hooked up to state-of-the-art Macintosh computers are perched close to the entrance, and the shop has maintained a Web site for more than two years. But sell on eBay? No way, says the prim, bespectacled Bernd Goeckler. "That sort of thing happens at a lower level of the business," he explains.

Things look more promising at Howard Kaplan Antiques, a dark, expansive shop around the corner on a busy street, where I'm greeted by a youngish, gaunt man encased in black, who looks smirkily hip enough to be CEO of one of the Silicon Alley start-ups only blocks away. But the question of online auctioning gets me brusquely turned away.

A morning spent hopping around this domain of \$35-a-square-foot storefronts sheltering million-dollar inventories fails to turn up a single antiques shop owner professing interest in selling on eBay or its competitors. Something else that fails to turn up in my presence: a single walk-in customer. Meanwhile, on this same morning, bids are pouring in on well over 5,000 antiques listed on eBay alone, items ranging from a piano stool (minimum bid: \$5.50) to a Maxfield Parrish architectural panel (minimum bid: \$35,000 -- so much for the "lower-level" theory). It seems a strange disconnect, but in fact it's par for the course, according to Dave Brennan, director of the Small Business Institute at the University of St. Thomas in St. Paul, Minn. "Most brick-and-mortar businesses just don't get it," he says. According to the U.S. Small Business Administration, 70% of small businesses have no Web sales capabilities whatsoever.

No Inventory? No Problem

Some microbusinesses operate successfully with no inventory, thanks to the fact that online-auction customers are reconciled to a lag of a week or more between placing a winning bid and receiving the item. A seller can wait until an order is in before actually purchasing the item that he or she has just sold, adding perhaps a harmless extra day or two to the lag time. **Tony Surtees**, general manager of the Commerce Group at Yahoo, told me about one seller who looks for low-priced items in antiques shops, puts holds on them, snaps pictures of them with a digital camera, and throws them up at auction online. If he gets his minimum price on an item, then he goes back to the store and buys it; otherwise he cancels the hold. Or here's what one watch seller states on its Yahoo cyberboutique: "AAA Jewelers ... is not an authorized representative of all the manufacturers whose watches and jewelry are offered for sale. ... To keep costs down, AAA Jewelers maintains a limited inventory and often obtains an item from its dealer network once an order is placed. In the vast majority of cases the item is shipped within 3-5 business days. ... Some items may not be available." I'm sure my local jeweler would be able to keep his costs down, too, if he could get away with telling customers that their watches would be in the store a mere five business days after they were paid for.